



Statement of the U.S. Chamber of Commerce

ON: Hearing on the Need for Comprehensive Tax Reform to
Help American Companies Compete in the Global Market
and Create Jobs for American Workers

TO: House Committee on Ways & Means

DATE: May 12, 2011

The Chamber's mission is to advance human progress through an economic,
political and social system based on individual freedom,
incentive, initiative, opportunity and responsibility.

The U.S. Chamber of Commerce is the world's largest business federation, representing the interests of more than 3 million businesses of all sizes, sectors, and regions, as well as state and local chambers and industry associations.

More than 96 percent of the Chamber's members are small businesses with 100 or fewer employees, 70 percent of which have 10 or fewer employees. Yet, virtually all of the nation's largest companies are also active members. We are particularly cognizant of the problems of smaller businesses, as well as issues facing the business community at large.

Besides representing a cross-section of the American business community in terms of number of employees, the Chamber represents a wide management spectrum by type of business and location. Each major classification of American business -- manufacturing, retailing, services, construction, wholesaling, and finance -- is represented. Also, the Chamber has substantial membership in all 50 states.

The Chamber's international reach is substantial as well. It believes that global interdependence provides an opportunity, not a threat. In addition to the U.S. Chamber of Commerce's 115 American Chambers of Commerce abroad, an increasing number of members are engaged in the export and import of both goods and services and have ongoing investment activities. The Chamber favors strengthened international competitiveness and opposes artificial U.S. and foreign barriers to international business.

Positions on national issues are developed by a cross-section of Chamber members serving on committees, subcommittees, and task forces. More than 1,000 business people participate in this process.

Chairman Camp, Ranking Member Levin, and Members of the Committee, the U.S. Chamber of Commerce greatly appreciates the opportunity to comment on the need for tax reform and issues related to global competitiveness.

INTRODUCTION

We live in an increasingly global economy. Technology advances have changed the way business works. Unfortunately, the U.S. tax code¹ has not kept pace. It is plagued by problems – including a too high tax rate, a bias against capital investment, an outdated worldwide system of taxation, and excessive complexity. Failure to act to address these problems could hurt the ability of American companies to compete, deter foreign investment in the United States, decrease capital investment, and result in American job losses.

COMPETITIVE CHALLENGES

For U.S. companies to compete in global markets, they need a level playing field. In 2011, the United States suffers the second highest corporate tax rate in the world. Moreover, the United States is the only major industrialized OECD country that continues to employ a worldwide system of taxation. This high tax rate and possibility of double taxation, while mitigated by provisions such as deferral and the foreign tax credit, harms the ability of U.S. companies to compete against foreign companies who face little or no home country tax.

The U.S. tax code is lagging sadly behind its worldwide competitors. First, the U.S. marginal corporate tax rate, at 35 percent, is completely out of step with other major industrialized OECD nations. As noted by the Tax Foundation,² a nonpartisan organization, “2011 marks the 20th year in which the statutory U.S. corporate tax rate has exceeded the simple average of the non-U.S. OECD nations and the twelfth year in which our rate has exceeded the weighted average OECD rate.”

Further, as noted in another Tax Foundation study,³ we not only shackle our businesses with high rates, but we have taken no action to lower our rate as other countries have acted. As the study notes, “[i]n the past four years alone, 75 countries have cut their corporate tax rates to make themselves more competitive.” Our major trading partners– Canada and Great Britain – have already taken steps to make themselves more competitive by dropping their corporate tax rates, while the United States has done nothing to reduce rates.

In addition to our high rates, we remain the last major industrialized OECD country with a worldwide system of taxation.⁴ As countries like Great Britain not only lower rates but shift to quasi-territorial systems of taxation, the United States continues to overburden American businesses. Other countries are shifting to more efficient and globally conducive systems of

¹ All references to the Code are to the Internal Revenue Code of 1986, as amended, and the regulations promulgated thereunder.

² See Tax Foundation, Fiscal Fact No. 261, Countdown to #1 : 2011 Marks 20th Year That U.S. Corporate Tax Rate Is Higher than OECD Average, available at <http://www.taxfoundation.org/publications/show/27100.html>.

³ See Tax Foundation, Special Report No. 191, Ten Reasons the U.S. Should Move to a Territorial System of Taxing Foreign Earnings, available at <http://www.taxfoundation.org/files/sr191.pdf>.

⁴ See id.

taxation, while we are standing by and doing little to help American companies compete, let alone win.

U.S. companies are disadvantaged by not only high rates and our system of taxing foreign source income, but also by the uncertainty that results from the temporary nature of so many crucial business tax provisions. Since 1986, the code has seen over 15,000 changes, and, as of last count at the end of 2010, contained 141 temporary provisions, such as the CFC look-thru rule active financing exception, which generally require annual renewal by Congress.⁵

We must do something to address our high corporate tax rates and antiquated system of taxing foreign source income to allow U.S. companies to compete globally. Further, we must act to address the temporary nature of our code to provide businesses the certainty to most effectively make business decisions.

UNIVERSAL IMPACT

The Interrelationship of Large and Small Businesses

Small and large businesses work together to help each other and to strengthen the U.S. economy. According to a September 2010 study,⁶ the supplier-buyer relationship between American small businesses and large U.S. companies is a basic and entrenched aspect of our economy. It notes that large companies “are major customers of small businesses and play a critical role in their growth and success.”

The study concluded that:

- “Parent operations of U.S. multinational companies buy nearly a quarter of all the goods and services they use as inputs in their production from U.S. small businesses – more than an estimated \$1.5 trillion annually; and
- Every \$1 billion in new exports by large U.S. companies would result in approximately \$174 million in new purchases of goods and services from America’s small businesses.”

This study makes abundantly clear that changes to the tax code that impact large businesses also impact the small businesses that provide goods and services to them. If we continue to maintain a tax code which harms the competitiveness and profitability of large U.S. companies, it is clear that we also negatively impact the smaller companies in their supply chains.

⁵ See, e.g., Hearing Statement of Senator Max Baucus (D-Mont.), Regarding Changes in the Tax Code since the 1986 Tax Reform Act, available at <http://finance.senate.gov/imo/media/doc/03012011%20Baucus%20Hearing%20Statement%20on%20Changes%20in%20the%20Tax%20Code%20since%201986%20Reforms.pdf>.

⁶ See “Business Roundtable Study Shows America’s Large and Small Businesses Critical Partners in Economic Recovery,” available at http://businessroundtable.org/uploads/news-center/downloads/SME_Study_Release_v17.pdf.

Impact of Reform on Small Businesses

In addition to small businesses being impacted because they operate as part of larger companies' supply chains, the Chamber believes Congress would be remiss to take action to reform the code for businesses operating in C corporation structures while ignoring those operating in passthrough form.

According to a recent study by Ernst & Young, more than 90 percent of businesses in the United States are organized as flow-through entities. That study also found that individual owners of flow-through entities paid 44 percent of all federal business income taxes between 2004 and 2008 and, moreover, that flow-through businesses employ 54 percent of the private sector work force in the United States.⁷ Flow-through businesses are a critical source of job creation and innovation in the United States that cannot be ignored in fundamental tax reform.

Under current law, the same top marginal income tax rate of 35% applies both to corporations and pass-through entities. In addition, business tax expenditures included in the code apply to both corporations and flowthrough businesses. If corporate tax reform takes place separate from individual tax reform, pursuant to which the corporate rate is lowered in exchange for the elimination or reduction of business tax expenditures, passthrough entities will lose the benefit of business tax expenditures without a corresponding rate reduction. Piecemeal corporate tax reform thus could have a negative financial impact on passthroughs, putting jobs at risk.

GUIDING PRINCIPLES

The Chamber believes that any changes to the tax code should adhere to the following principles:

- Tax reform legislation should lower the corporate tax rate to a level that will enable U.S. businesses to compete successfully in the global economy, attract foreign investment to the United States, increase capital for investment, and drive job creation in the United States. Congress should consider the impact of a corporate rate reduction on passthrough entities.
- In addition to reducing tax rates, tax reform should eliminate the bias in the current U.S. tax system against capital investment. Capital investment should be expensed or recovered using a capital cost recovery system that provides the present value equivalent to expensing with due regard to the impact the system may have on cash flow.
- In the international arena, the current worldwide tax system should be replaced with a territorial system for the taxation of foreign source income to enable U.S. businesses to compete successfully in the global economy, as well as domestically against foreign firms, and to promote economic growth domestically.
- Changes should be permanent to ensure certainty for businesses striving to expand, create jobs, and remain competitive in the United States and abroad.
- Fundamental reform should take place in the near-term, and Congress should not, in the interim, adversely change the current tax policy.

⁷ Carroll and Prante, "The Flow-Through Business Sector and Tax Reform," April 2011, available at <http://www.scorp.org/wp-content/uploads/2011/04/Flow-Through-Report-Final-2011-04-08.pdf>.

- Congress preferably should pass comprehensive tax reform legislation; conversely, Congress should avoid undertaking tax reform on a piecemeal basis.
- Congress should enact simple, predictable and easy to understand tax rules to improve compliance and reduce the cost of tax administration.
- Tax reform legislation should ensure industry-specific neutrality and avoid special tax benefits or penalties targeted to one industry versus another. Tax reform should allow the marketplace, not the tax system, to allocate capital and resources.
- Comprehensive tax reform should include realistic transition rules to provide adequate time for implementation and help minimize economic hardships businesses may encounter in transitioning to the new tax system.

CONCLUSION

The Chamber thanks Chairman Camp, Ranking Member Levin, and Members of the Committee for the opportunity to comment on tax reform and global competitiveness. As Congress considers possible fundamental tax reform, the Chamber believes lowering the corporate tax rate, shifting to a territorial tax system, and addressing the uncertainty of our code are critical matters. Further, the Chamber believes that any tax reform effort must consider the role small businesses play in our global economy.